

Kentucky Agriculture Finance Corporation

Meeting Minutes

September 12, 2003

The Kentucky Agriculture Finance Corporation met at 9:30 am on September 12, 2003 in the Capitol Building in Frankfort, Kentucky.

Members Present:

Ms. Jane Jones; Mr. Dwight Price, designee for Gordon Duke; Dr. Harold Benson; Ms. Annette Crawford Walters; Mr. Wayne Hunt; Mr. Bob D. Proffitt; Commissioner Billy Ray Smith; Mr. Doug Lawson

Members Absent:

Mr. Billy Joe Miles; Ms. Sandy Ross; Mr. Billy Hurd; Mr. Charles Miller

Governor's Office of Agricultural Policy Staff Present:

David Bratcher; Bill Hearn; Bill McCloskey; Joel Neaveill; Edith Fultz

Guests:

Mr. Mark Farrow, General Council Kentucky Department of Agriculture
Ms. Ann Stewart, Kentucky Department of Agriculture
Kathi Marshall, Governor's Office for Policy and Management
Shana Herron, Community Farm Alliance
Biff Baker, Legislative Research Commission

Commissioner Billy Ray Smith - announced that the press was notified of this meeting and asked the secretary to call the roll. Guests introduced themselves to the board.

Commissioner Smith – called for approval of the Minutes of the August 8th meeting. Annette Crawford Walters noted a needed correction in the committee lists. Bob Proffitt made a motion to approve the minutes with the needed modifications; Wayne Hunt seconded the motion. The minutes were approved.

Old Business:

David Bratcher – reminded the Board of the visit from Butch Dunsmore from the Farm Service Agency (FSA) at the August 8th meeting at which time the board agreed to move forward to become an FSA-approved lender. The Washington office of FSA has raised the question of how we are regulated. Mr. Bratcher explained we are subject to

audit by the State Auditor and in our audit engagement we will require a management review by the Auditor. The FSA Washington staff has taken this into consideration and likely will require the agreement between KAFC and FSA to include the management review as a condition of the audit. FSA also was pleased to hear that the Board members include active FSA lenders. Three other states, Vermont, California and North Carolina, are also FSA-approved guarantee lenders. Mr. Dunsmore feels that if these states can be approved for this program, KAFC also will be, especially since the other state lenders are not regulated except by audits.

We haven't heard anything definitive from Washington at this time but believe there will be an agreement in place by the September meeting. Therefore guideline discussion this morning will assume that KAFC will be an FSA approved lender. Annette Crawford Walters asked if FSA is recommending a bad debt reserve. Mr. Bratcher responded that of discussion has not occurred.

Mr. Bratcher – introduced Dwight Price from the Office of Financial Management who will be KAFC's liaison with Farmers Bank.

Dwight Price – shared copies of the agreement that is ready to be executed to engage the Office of Financial Management in the actual investments of our funds once the funds are placed in Farmers Bank. He explained the MARS System, which is the state accounting system. OFM is recommending that KAFC stay with the state's contract with Farmers Bank. He told us they have met with Farmers Bank staff and they are agreeable to adding an addendum to the state's contract, adding another account. Mr. Bratcher handed out an example of the fee structure.

Mr. Price - explained how the Office of Financial Management invests state funds and explained they could easily include KAFC's funds in state investments to build a portfolio for us. Mr. Bratcher pointed out that the maximum annual fee would be \$10,000. Commissioner Smith asked if this is going to be a separate portfolio from the rest of the state. Mr. Price responded that it will be separate and explained. Mr. Bratcher explained that we will have two separate accounts at Farmers Bank, the account that has the \$20,000,000 initially deposited and to the extent that we have any counties that elect to do revolving loan funds, a separate account that will be an aggregating account for all of the particular counties' funds. KAFC we will account for each one of the respective county loan funds individually but at Farmers Bank those funds will be in the one account. At this time no county has officially adopted the revolving loan fund program. Mr. Price explained the market value fee. There was further discussion by the group.

Mr. Bratcher - entertained a motion to authorize Commissioner Smith as our Chairman to execute the agreement with the Office of Financial Management and the Investment Commission to invest our money and an affirmation that we can go forward with the Farmers Bank agreement. Harold Benson made the motion; Mr. Lawson seconded the motion. The motion passed.

Mr. Bratcher distributed copies of the draft agreement between the KAFC and the ADB. He explained that if we elect to add another program we would have to go back to the ADB for their approval although KAFC will be making periodic reports to KAFC on a regular basis to keep them informed of our activities.

He explained that our intent and representation to the ADB has been that this is going to be a self-supportive organization. Our hope is to invest the \$20,000,000 and use our earnings to pay administrative expenses. There are monthly fees to Farmers Bank whether we have earnings or not. One of the questions to be resolved is who will actually pay Farmers Bank for the fees associated with individual county accounts in terms of the management of those funds. There should be some latitude to dip into the corpus of the funds for minimal administrative expenses.

He told us that one of the ADB members is an attorney who has requested input on this agreement. Once this is done and the agreement is in final form Commissioner Smith and Gene Royalty, representing KAFC and ADB, respectively, will sign at which point in time the \$20,000,000 will move to Farmers Bank.

Mr. Lawson - asked what events might trigger the termination clause in the agreement. Mr. Bratcher responded, inactivity on the part of this Board to sign the agreement. He explained that this is more for the dispersing of the \$20,000,000 than it is for default under the agreement. He explained further. There were comments and discussion.

Mr. Lawson - explained that the Kentucky Bankers Association meeting had to be rescheduled due to the death of the Director. He told us that materials have been sent out and they are somewhat informed.

New Business:

Mr. Bratcher – presented a draft of the Program Guidelines for the KAFC and invited comments for changes or needed corrections. There was group discussion with some changes suggested.

Mr. Lawson - raised the issue of bank reporting and needed software. Mr. Bratcher responded saying our operations committee needs to advise us of the types of software we need. He added that he hopes to avoid bank fees for servicing of KAFC's loans. Mr. Lawson - responded that with the area of Investment Fund for Agriculture we may be better off to allow a fee, have the bank handle the transactions and require reporting from them. Ms. Walters concurred. Mr. Bratcher questioned if we need to include in these guidelines, that reasonable servicing fees would be allowed. There were further comments and the consensus of the board was to include that provision.

Mr. Bratcher commented that the one thing that we may wish to service our direct loans, recognizing that right now the Young Farmer Program will be our only direct loan program. Depending on volume we may not need as complicated software as a commercial lender, but we will need something beyond excel to do the spreadsheets,

etc. As KAFC intends to sell these loans off we will want to assure any software has capability of adequate reporting to the investors to whom we will be remitting periodic payments.

Mr. Bratcher - addressed the issue of making a change in the interest rate adjustment in the guidelines. Mr. Lawson suggested review annually and adjust according to the original promissory note. There was further comment and discussion.

Wayne Hunt - revisited the question of establishing ceilings for amounts of money in each program. Mr. Bratcher responded that at this point in time it is his opinion that we should wait until we have a better understanding of where the demand is going to be.

Discussion then moved to guidelines for each of the three program areas:

Investment Fund for Agriculture

Board members concurred with the maximum million-dollar buy-down provision in the As to the term of the investment the board concurred with a maximum 7- year term for non real estate investments, but preferred 20 years for real estate, with a blended term for investments in loans financing both equipment and real estate. Mr. Lawson noted that we would want to shorten our term with our low interest rate portion. There was further discussion and comments from members of the group.

Mr. Lawson suggested a 200 basis point discount off the local lender's rate. There was group discussion with agreement on this. Mr. Bratcher stated that the interest rate will be a 200 basis point discount below the local lenders rate.

Jane Jones - commented that Farm Credit offers fixed rates for 5 – 20 years and asked if we are going to commit for that length of time. Mr. Bratcher responded that we are going to lock it for our term. Ms. Jones asked if this is going to be profitable. Mr. Lawson responded commenting that we are going to work off the bank's expertise of what is and what is not a profitable endeavor.

There was considerable discussion regarding the nature of projects being financed. As drafted the guidelines could allow for financing of expansion projects related to production agriculture. Mr. Bratcher asked if the language in the second bullet encapsulates what the Board thinks this program should be or should it be worded differently. He asked for further comments on these guidelines explaining that when we disseminate this to the community we want everyone to understand where we want to take this program. There was group discussion.

Harold Benson – asked if any portion of this will speak to the initiative of changing the face of agriculture, as we know it thereby enhancing the likelihood of greater success for young farmers. Mr. Bratcher offered his opinion that the two areas that come closest to that is the first two. He mentioned the investment fund for agriculture being used as a

potential incentive for those who want to do value added. He used the goat milk company as an example. He also explained that under the statute, we cannot purchase stock. Dr. Benson commented further about this need. Mr. Hunt explained that with the ADF we have created a lot of initiative. We now have the opportunity to bring production and marketing to this state. Mr. Bratcher commented that what we would like to see is the farmers themselves not only producing and selling but also sharing in the profits of the venture. There was further discussion.

Ms. Jones -commented this program needs to promote something special. Mr. Bratcher asked if the guideline should read KAFC funds will be made available only for projects that add value to agricultural commodities. He emphasized that this is very restrictive. There was further discussion. Mr. Bratcher asked the group if they are comfortable with making this that restrictive. Ms. Walters commented that we want to entice industries to come into the state to utilize our product. She stressed that we need to have this as our emphasis. Mr. Hunt stated that if we put land into this we will quickly use the fund up. He commented further. There was group discussion.

Dr. Benson - commented on the importance of offering some incentive to keep people in agriculture.

Mr. Bratcher – stated that in the future we might say that enabling legislation isn't broad enough. Part of the difficulty is that today we don't know how big KAFC could become. Regardless KAFC should not be just another farm lender. For example, the ADB has a pending application from a group of farmers in the south central part of the state that wants to get into a soybean extrusion facility. He explained that this is the kind of direction he would like to see this program going. Mr. Lawson emphasized that our focus needs to be on the value added section. He commented further saying that we need to remember our purpose as we review applications and make sure that the things we fund meet our purpose and our goals.

Mr. Bratcher – summarized this section of the guidelines. There was group discussion. Suggested changes follow.

1. Term of the investment would equal the term of the lenders loan. The maximum term for the transaction will not exceed 7 years for non real estate financing and 20 years for real estate financing.
2. Interest rate will be a 200 basis point discount below the local lenders rate, never less than 4%.
3. The interest rate will be reviewed annually on the anniversary of the inter-creditor agreement and may be adjusted based on the original lenders loan rate. Reasonable servicing fees may be allowed to the local lender.

Agricultural Endeavors Lease program:

Mr. Bratcher - explained this program. He also explained KRS 103 and the incentives we could provide through this law. There was group discussion.

Commissioner Smith – asked if there will be anything that would preclude this Board from bonding the monies that we have put into real estate, value added facilities or economic development and using these proceeds to fund the other two programs. Mr. Hunt commented that we want to do some of all of these programs.

Because he needed to leave to make a speaking engagement in Campbellsville, Commissioner Smith asked Ms. Walters, as Vice Chair, to preside in his absence.

Young Farmer Financing Program:

Mr. Lawson -asked if we have a restriction or can we get an FSA guaranteed loan to a farmer for an expansion and can we do this under the investment fund, have a FSA guarantee and sell that portion off.

Mr. Bratcher – explained that we have written this section in compliance with the statute, as it exists. He explained that if we want to do another FSA guarantee program for non - young farmers we could do that subject to a change in statute. There was group discussion with the general consensus being that this doesn't need further definition. Mr. Bratcher commented further that he believes that every loan we do for the first 6 months to a year needs to be scrutinized by the KAFC board.

Ms. Walters – voiced concern about the point stating that applicant must not be able to acquire funds elsewhere. Mr. Bratcher explained that this is a FSA requirement. There was group discussion.

Mr. Hunt - noted that there is no mention of tobacco dependent counties. Mr. Bratcher explained that in our application to the ADB we stated that our emphasis was going to be on tobacco dependent counties. He added that we don't want to lose sight of this. He commented further that this is going to be brought up every time we go to the oversight committee meeting. He explained that our initial focus will be on northeast Kentucky. There was group discussion with the suggestion of adding a bullet that states, "Emphasis will be on loans from heavily impacted tobacco areas". Mr. Bratcher reminded the group of the change to be made in the last line of the italicized portion. The change will read, "provided KAFC's loan will be guaranteed by FSA".

Ms. Walters - entertained a motion to approve the amended program guidelines. Dr. Benson made the motion; Mr. Lawson seconded the motion. The motion passed.

Next Meeting Date:

The next meeting is scheduled for 9:30 am on October 10, 2003

Adjourn:

The meeting adjourned at 12:00pm